1. INTRODUCTION

In the UK, the cornerstone of the corporate governance regime is the UK Corporate Governance Code published by the Financial Reporting Council. The UK Corporate Governance Code sets out a series of main principles of good governance together with supporting principles and additional provisions covering the key elements of effective board practice - leadership, effectiveness, accountability, remuneration and relations with shareholders.

The UK Corporate Governance Code applies to companies with a premium listing of equity shares and does not apply directly to AIM companies. However, it is clearly essential that smaller quoted companies (including AIM companies) establish and maintain appropriate and effective corporate governance arrangements. Accordingly, in order to provide guidance to such companies on best governance practice, the Quoted Companies Alliance (the **"QCA"**), a non-profit organisation which represents the interests of smaller quoted companies, published its own corporate governance guidelines. The latest version of these guidelines takes the form of the Corporate Governance Code for Small and Mid-Size Quoted Companies 2013 (the **"QCA Code"**). The QCA Code adopts key elements of the UK Corporate Governance Code and other relevant guidance and applies them to the needs and particular circumstances of small and mid-size quoted companies on a public market.

In addition, the National Association of Pension Funds has published its own Corporate Governance Policy and Voting Guidelines for Smaller Companies (November 2012) (the **"NAPF Smaller Company Guidelines"**). The NAPF Smaller Company Guidelines are primarily designed for companies listed on the AIM market and require the boards of AIM companies to be familiar with the main principles of the UK Corporate Governance Code and to seek to apply them as appropriate to their individual circumstances.

The QCA Code is described in detail in paragraph 2 of this Memorandum and, in view of the fact that many of its elements are derived from the UK Corporate Governance Code, a summary of the latter is included in paragraph 3. Finally, paragraph 4 contains a description of the NAPF Smaller Company Guidelines.

2. THE QCA CORPORATE GOVERNANCE CODE

2.1 The QCA Principles

The QCA considers that the objective of corporate governance is to deliver growth in long term shareholder value by maintaining a flexible, efficient and effective management framework within an entrepreneurial environment. The QCA Code sets out 12 principles which will enable companies to achieve this objective. The first six principles focus on the delivery of growth in long term shareholder value and the remaining six principles are aimed at the maintenance of a flexible, efficient and effective management framework within an entrepreneurial environment.

These 12 principles together with a summary of how they are to be applied are set out below:

(a) *Principle 1: Setting out the vision and strategy*

The board should articulate a shared view of the company's vision and strategy and ensure that it is communicated internally and externally. This view must include detail of the company's objectives, the period in which those objectives are to be achieved and what is required to achieve those objectives.

(b) *Principle 2: Managing and communicating risk and implementing internal control*

The board is responsible for putting in place and communicating a sound system to manage risk and implement internal control. When setting strategy, the board must determine the extent of exposure to the critical risks the company is willing and able to bear.

(c) *Principle 3: Articulating strategy through corporate communication and investor relations*

There should be a healthy dialogue between the board and all shareholders so that shareholders are in a position to make informed decisions. Appropriate communication and reporting structures should exist between the board and all constituent parts of the shareholder body so as to facilitate both the communication of shareholders' views to the board and shareholders' understanding of the unique circumstances and constraints faced by the company.

(d) *Principle 4: Meeting the needs and objectives of shareholders*

The board should ensure it has a good understanding of the needs and expectations of shareholders and also the motivation behind shareholder voting decisions. In particular, the views of shareholders should be ascertained before a potentially controversial or unusual proposal is put to them.

Where the company has a dominant shareholder, it is important to ensure that the views of the minority shareholders are heard and their interests protected. A relationship agreement with the dominant shareholder may need to be put in place for this purpose.

(e) *Principle 5: Meeting stakeholder and social responsibilities*

As part of its governance processes, the board should consider the company's impact on society, the community and the environment. Every company should consider its corporate social responsibilities (**"CSR"**) and any CSR policy should identify relevant social and environmental issues and show how these are integrated into the company's strategy. The integration of CSR into strategy will help create long-term value and reduce risk to shareholders and other stakeholders.

(f) *Principle 6: Using cost-effective and value-added arrangements*

Given the cost involved in delivering effective corporate governance, it is vital to ensure that the governance arrangements adopted are effective and proportionate and that the decision-making processes are clear and efficient. There should be a clear understanding between the board and shareholders of how value is enhanced and abuses prevented through effective corporate governance. Where relevant, key performance indicators should be published.

(g) *Principle 7: Developing structures and processes*

The company should determine the governance structures and processes appropriate to it, based on corporate culture, size and business complexity as well as taking into account the capacity and appetite for risk and the tolerances of the company. These structures should evolve over time in line with the company's strategy and business.

(h) *Principle 8: Being responsible and accountable*

Responsibility for corporate governance lies with the chairman who must therefore determine where responsibility lies within the company for the achievement of key outputs.

(i) *Principle 9: Having balance on the board*

The board should not be dominated by one person or a group of people. It must not be so large that it does not operate efficiently nor must it be so small that it is ineffective. The board should have a balance of executive and non-executive directors and should have at least two independent non-executive directors.

(j) *Principle 10: Having appropriate skills and capabilities on the board*

The board must have an appropriate balance of functional and sector skills and experience and should be supported by committees (audit, remuneration, nomination and others) that have the necessary character, skills and knowledge to discharge their duties and responsibilities effectively.

(k) *Principle 11: Evaluating board performance and development*

The board should periodically review its performance (as well as the performance of its committees and individual board members). Performance appraisal may include external review.

The board should ensure that it possesses the skills and experience to meet present and future business needs. Ineffective directors (whether executive and non-executive) must be identified, supported so that they become effective or, if that is not possible, replaced.

Membership of the board should be periodically refreshed, regardless of performance issues. Succession planning is very important. No member of the board should become indispensable.

(l) *Principle 12: Providing information and support*

All members of the board and its committees should be provided with high quality information in a timely manner so that they can properly assess the matters requiring a decision or insight. Non-executive directors should have access to all information they require and to external advice as necessary.

2.2 Characteristics of an effective board

According to the QCA Code, an effective board is a board which:

- works as a team led by the chairman;
- has a chairman who demonstrates his responsibility for corporate governance;
- develops and clearly articulates the strategy of the company;
- evaluates its performance and acts on the conclusions;
- regularly informs and engages with shareholders; and
- has a balance of skills, experience and independence.

These six characteristics are considered further below:

(a) *Working as a team led by the chairman*

A well-functioning board is a team led by the chairman and not by any member of the executive. Board members must be carefully selected and managed, taking into account group dynamics and the medium to long term needs of the business.

(b) *Having a chairman who demonstrates responsibility for corporate governance*

The primary responsibility of the chairman is the delivery of a company's corporate governance model. He must be adequately separated from the day-to-day business so that he can make independent decisions and, save in exceptional circumstances, he should not also serve as chief executive. It is important for the chairman to be visible in his role (for example, through attendance at results presentations and meetings with shareholders).

(c) *Developing and clearly articulating the strategy of the company*

Each director should be able to explain the company's strategy and how it will be delivered, how the corporate governance structure facilitates decision-making and why that structure is appropriate for the company.

Strict compliance with corporate governance guidelines is not compulsory but any non-compliance must be properly justified and the board must provide a clear and concise explanation as to why such non-compliance is appropriate for the company and is in the best interests of shareholders.

(d) *Evaluating board performance and acting on the conclusions*

It is part of the role of the chairman to maximise the effectiveness of each director. Open and honest board evaluation should facilitate an improvement in board performance.

Disclosure regarding board evaluation should focus on objectives and targets for improving performance rather than simply describing the process followed. It is also important to have an effective induction process for new directors and regular training in areas where further development needs are identified.

(e) *Regularly informing and engaging with shareholders*

The chairman must ensure that the company has in place effective lines of communication with all shareholders. Communication should encourage both discussion and feedback. Positive communication and healthy discussion will enable a shareholder to discharge its stewardship responsibilities and enable a company to benefit from the insight and market expertise of well-informed shareholders. The engagement with shareholders should involve a discussion whether directors should be subject to annual re-election.

(f) *Having a balance of skills, experience and independence*

The composition of the board should be such that it has the right mix of skills and experience to deliver the strategy of the company for the benefit of shareholders as whole. The promotion of greater board diversity (including gender diversity) should be the focus of serious consideration.

In determining the independence of a non-executive director, the key considerations are the individual's approach to the role and his ability to behave effectively and independently. The issue of independence is considered further in paragraph 2.3.

2.3 **Independence**

The QCA recognises that small and mid-size companies may find it difficult meet the independence criteria set out in the UK Corporate Governance Code (see paragraph 3.3(a) below) and emphasises the importance for the boards of such companies to foster an attitude of independence of character and judgement.

A company should have at least two independent non-executive directors. The chairman may count as one of the independent directors provided he was independent at the time of appointment. A company should explain in its annual report and discussions with shareholders the reasons why the relevant directors are considered to be independent. The QCA identifies two particular circumstances which might, or might appear to, affect a director's judgement and bring his independence into question:

(a) the first circumstance is where the director is financially dependent on his relationships with the company. Whilst remuneration in shares does not of itself impair independence, non-executive directors should not normally participate in share option schemes. Where performance-related remuneration is under consideration, shareholder support must be obtained; and

(b) the second circumstance is where the director is, or represents, a major shareholder. Where a board includes a director associated with a major shareholder, shareholders should be provided with an explanation of the reasons for the relevant individual sitting on the board, details of any relationship agreement in place and the particular skills and experience the relevant individual brings to the board.

2.4 Roles and responsibilities

The QCA Code briefly sets out the various roles of those concerned with the governance of a company:

(a) *Chairman*

The role and responsibilities the chairman, whose governance role is key, are outlined in paragraph 2.2.

(b) *Senior independent director*

The appointment of one of the independent non-executive directors to the role of senior independent director is a requirement of the UK Corporate Governance Code and all companies should consider whether it is appropriate to appoint one.

The role of the senior independent director is to act as a sounding board for the chairman and the other directors and to serve as an intermediary for shareholders and the other directors when they have concerns that cannot be raised through the normal channels. The senior independent director would also typically be expected to chair an annual meeting of the non-executives to assess the chairman's performance and take a lead role on succession planning (in particular, as regards the search for a new chairman).

(c) *Non-executive directors*

The role of the non-executive directors in the determination and articulation of strategy is crucial. They have a responsibility both to challenge and inspire executive directors with a view to ensuring the implementation of the agreed strategy and the operation of the business with reference to the risk management framework.

Independence of non-executive directors is critical in enabling them to provide appropriate oversight and to perform the role expected of them. Non-executive directors should expect to undergo a formal appointment process and a structured induction process (including meetings with shareholders), to commit an appropriate amount of time to the role (and to be available to meet shareholders), to serve on board committees, to receive training and development and to be subject to regular performance assessment.

(d) *Executive directors*

The executive directors are responsible for the delivery of the company's business within the strategy set by the board. All executive directors should operate in an open and transparent way, keeping the other members of the board up to date with operational risks and issues.

(e) *Members of the audit committee*

The audit committee plays a crucial role in providing shareholders with confidence in the annual report and accounts and other relevant public announcements. The committee should challenge both the external auditors and company management and review the need for internal audit.

(f) *Members of the remuneration committee*

Remuneration arrangements should be aligned with and support the implementation of company strategy and effective risk management. The remuneration committee is responsible for ensuring that this principle is applied and for taking into account the views of shareholders. Remuneration policy should be designed to motivate the right behaviours.

(g) *Members of the nomination committee*

Whilst some small and mid-size quoted companies will establish a dedicated committee, others will choose to leave nomination matters to the full board.

Where there is a dedicated nomination committee, the committee should work closely with the board and the chairman to identify the skills and experience needed for the next stage in the company's development. It should keep a close eye on succession plans and the possible internal candidates for future board roles. If necessary, the committee should support the chairman in the removal of underperforming directors.

(h) *Company secretary*

The company secretary plays a vital role in ensuring good governance and legal and regulatory compliance. His responsibilities typically include assisting the chairman in preparing for and running effective board meetings, circulating relevant information to board and committee members in a timely manner, acting as a conduit for the directors (in particular, the non-executive directors) into the workings of the company and acting as the link between the company and shareholders on matters of governance and investor relations.

The company secretary may, from time to time, have to act as a confidential sounding board for one or more of the directors and, in view of this sensitive role, it may be difficult for the company secretary also to be a director.

(i) *Shareholders*

Shareholders should take an active interest in the corporate governance of each company in which they have invested, giving careful consideration to disclosures made by the company and reaching reasoned judgments on a case-by-case basis. If concerns arise, shareholders should engage with the company.

2.5 **Demonstrating good corporate governance and minimum disclosures**

The QCA emphasises that good disclosure and open dialogue are necessary in order to achieve the right level of governance and to maintain trust between the board and a company's shareholders. The company should publish an annual corporate governance statement explaining how it achieves good governance and the challenges it faces in doing so. The statement should be included in the company's annual report and accounts or, failing that, made available on its website. The corporate governance statement should, as a minimum, explain how each of the 12 principles of the QCA Code is put into practice by the company.

The QCA Code indicates that, as part of the company's explanation of how it achieves good governance, certain prescribed matters should be disclosed in its annual report and accounts or on its website.

(a) *Annual report and accounts*

The following information should be included in the company's annual report and accounts:

(i) a report by the chairman of how the QCA Code is applied and how such application supports the company's long-term success and its strategy for growth;

(ii) an audit committee report explaining the major tasks undertaken and demonstrating independent oversight of both management and external auditors. The report should include:

- details of the significant issues considered by the committee in relation to the financial statements and how these issues were addressed;
- an explanation of how auditor objectivity and independence is safeguarded (particularly if the auditor provides significant non-audit services).

If the audit committee also operates as the risk committee (because there is no designated risk committee), there should also be a description of how this role has been undertaken;

(iii) a remuneration committee report explaining how remuneration policy and practice align with the company's strategy;

(iv) the identity of all the directors, their roles and committee memberships;

(v) a description of the relevant skills and experience that the executive and non-executive directors bring to the board;

(vi) the identity of those directors considered to be independent together with an explanation of the reasons for their independence (focusing, in particular, on any circumstances which may impair their independent status);

(vii) a brief description of the work of each committee and its role, responsibility and accountability;

(viii) the number of meetings of the board and each committee held during the year and the attendance records of each director;

(ix) a summary of the systems of risk management and internal control and the uncertainties facing the business together with an explanation of how risks align with the company's strategy, linking into key performance indicators, remuneration policies and corporate responsibility activities; and

(x) a description of the performance evaluation procedures for each director, the board as a whole and each committee, focusing on their objectives and outcomes together with a summary of how evaluation procedures have evolved from previous years, the results of the evaluation and action taken or planned as a result.

(b) Additional disclosures on the company's website

The following additional information should be made available on the company's website:

(i) a summary of information received by the board and by individual committees;

(ii) a clear articulation of the company's strategy;

(iii) a description of the roles and responsibilities of the chairman, chief executive and, if applicable, the senior independent director;

(iv) a list of the types of decision reserved for the board;

(v) the terms and conditions of appointment of non-executive directors;

(vi) the terms of reference of the audit and remuneration committees;

(vii) the terms of reference of the nomination committee (or, if there is no separate nomination committee, an explanation of the processes by which the board determines nomination and senior appointment matters);

(viii) an explanation of the role of any external advisers to the board or its committees (in particular, the remuneration committee) and any internal advisory responsibilities (such as the roles performed by the company secretary and the senior independent director in advising and supporting the chairman). If the company secretary is also a director, an explanation for this;

(ix) the annual report and other governance-related material (including notices of general meetings over the last three years); and

(x) the results of any shareholder votes including, in the case of a vote on a show of hands, details of the votes by proxy received by the company (including abstentions or votes withheld) and, in the case of a vote on a poll, details of the actual votes (including abstentions or votes withheld). This information should be reported as soon as practical after the meeting or (as the case may be) after the poll.

3. THE UK CORPORATE GOVERNANCE CODE

3.1 Introduction

This section of the Memorandum contains a summary of the UK Corporate Governance Code which, as stated above, applies to companies with a premium listing of equity shares. The latest version of the UK Corporate Governance Code is the September 2014 version which applies to accounting periods beginning on or after 1 October 2014.

The UK Corporate Governance Code consists of 18 Main Principles of good governance which are developed and amplified through a series of Supporting Principles and more detailed Code Provisions. In this summary, the Main Principles are set out in full (in bold text). Each Main Principle is then followed by a short summary drawing attention to key elements of the Supporting Principles and Code Provisions relevant to that Main Principle.

3.2 Leadership

(a) The role of the board (A.1)

Every company should be headed by an effective board which is collectively responsible for the long-term success of the company.

The board's role is to provide entrepreneurial leadership of the company within a framework of prudent and effective controls which enables risk to be assessed and managed. It is the responsibility of the board to set the company's strategic aims, to ensure that the necessary resources (both financial and human) are in place for the company to meet its objectives and to review management performance.

All directors must act in what they consider to be the best interests of the company, consistent with their statutory duties.

The board should meet sufficiently regularly to discharge its duties effectively and there should be a formal schedule of matters specifically reserved for its decision. A statement of how the board operates should be included in the annual report.

(b) Division of responsibilities (A.2)

There should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. No one individual should have unfettered powers of decision.

The roles of chairman and chief executive should not be exercised by the same individual. There should be a clearly established, written and board-approved division of responsibilities between the two roles.

(c) The chairman (A.3)

The chairman is responsible for leadership of the board and ensuring its effectiveness on all aspects of its role.

The Code places great emphasis on the role of the chairman. He is responsible for setting the board's agenda and ensuring that adequate time is available for discussion of all agenda items, in particular strategic issues. He is also required to promote a culture of openness and debate by facilitating the effective contribution of non-executive directors and ensuring constructive relations between executive and non-executive directors. It is also his responsibility to ensure that the directors receive accurate, timely and clear information and to ensure effective communication with shareholders.

The chairman should on appointment meet the criteria for independence (see paragraph 3.3(a) below). A chief executive should not go on to be chairman of the same company. If, exceptionally, the board agrees to this, it should consult major shareholders in advance and explain its reasons to shareholders.

(d) **Non-executive directors (A.4)**

As part of their role as members of a unitary board, non-executive directors should constructively challenge and help develop proposals on strategy.

The key responsibilities of non-executive directors include scrutinising management performance in meeting agreed goals and objectives, monitoring the reporting of performance, satisfying themselves on the integrity of financial information and that financial controls and risk management systems are robust and defensible and determining appropriate levels of remuneration of executive directors. They also have a key role in the appointment and removal of executive directors and in succession planning.

One of the independent non-executive directors should be appointed to be the senior independent director whose role is to provide a sounding board for the chairman, to serve as an intermediary for the other directors when necessary and to be available to shareholders if they have concerns.

3.3 **Effectiveness**

(a) **The composition of the board (B.1)**

The board and its committees should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively.

The board should include an appropriate combination of executive and non-executive directors (and, in particular, independent non-executive directors) so as to ensure that no individual or small group of individuals can dominate the board's decision-taking.

The board should identify in the annual report each non-executive director whom it considers to be independent. Final judgment as to the independence of a director is a matter for the board. In essence, a director is considered independent if the board determines that the director is independent in character and judgment and there are no relationships or circumstances which are likely to affect, or could appear to affect, the director's judgment. The relationships and circumstances which may affect a director's judgment include the situation where a director:

- has been an employee within the last 5 years;
- has, or has had within the last 3 years, a direct or indirect material business relationship with the company;
- has received or receives additional remuneration from the company apart from a director's fee, participates in the company's share option or a performance-related pay scheme or is a member of the company's pension scheme;
- has close family ties with any of the company's advisers, directors or senior employees;
- holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;
- represents a significant shareholder; or
- has served on the board for more than 9 years from the date of first election.

Except for smaller companies (that is, companies below the FTSE 350 throughout the year immediately prior to the reporting year), at least half the board (excluding the chairman) should comprise independent non-executive directors. Smaller companies should have at least two independent non-executive directors.

(b) **Appointments to the board (B.2)**

There should be a formal, rigorous and transparent procedure for the appointment of new directors to the board.

Board appointments should be made on merit, against objective criteria and with due regard for the benefits of diversity on the board (including gender). The board should satisfy itself that plans are in place for an orderly succession for appointments to the board and senior management.

A nomination committee should be established to lead the process for board appointments and make recommendations to the board. A majority of its members should be independent non-executive directors and its chairman should be the chairman (but not when the committee is dealing with the appointment of a successor to the chairmanship) or an independent non-executive director.

Non-executive directors should be appointed for specified terms subject to re-election. Any term beyond six years should be subject to particularly rigorous review.

A description of the work of the nomination committee should be included in the annual report. This section should also include a description of the board's policy on diversity.

(c) **Commitment (B.3)**

All directors should be able to allocate sufficient time to the company to discharge their responsibilities effectively.

The Code Provisions emphasise, in the context of the appointment process, the need for the chairman and the non-executive directors to have sufficient time to meet what is expected of them.

The board should not agree to a full-time executive director taking on more than one non-executive directorship (or the chairmanship) of a FTSE 100 company.

(d) **Development (B.4)**

All directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge.

The Code emphasises the need for directors continually to update their skills and the knowledge and familiarity with the company required to fulfil their role on the board and its committees. The company must provide the necessary resources for developing and updating its directors' knowledge and capabilities.

To function effectively, all directors need appropriate knowledge of the company and access to its operations and staff.

New directors should receive a full, formal and tailored induction on joining the board (which should include meeting major shareholders). The chairman should regularly review and agree with each director their training and development needs.

(e) **Information and support (B.5)**

The board should be supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties.

The Code emphasises the importance of good information flows within the board and its committees and between senior management and non-executive directors.

The board should ensure that directors, especially non-executive directors, have access to independent professional advice at the company's expense where they judge it necessary to discharge their responsibilities as directors.

All directors should have access to the advice and services of the company secretary.

(f) **Evaluation (B.6)**

The board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors.

This evaluation should consider the balance of skills, experience, independence and knowledge of the company on the board, its diversity, including gender, how the board works together as a unit, and other factors relevant to its effectiveness.

The chairman should act on the results of the performance evaluation by recognising the strengths and addressing the weaknesses of the board. Where appropriate, this will involve proposing changes to the composition of the board.

The non-executive directors, led by the senior independent director, should be responsible for performance evaluation of the chairman, taking into account the views of executive directors.

The annual report should include a statement regarding how the performance evaluation of the board, its committees and individual directors.

(g) **Re-election (B.7)**

All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance.

All directors of FTSE 350 companies should be subject to annual election by shareholders. All other directors should be subject to election by shareholders at the first annual general meeting after their appointment and to re-election thereafter at intervals of no more than three years. Non-executive directors who have served longer than nine years should be subject to annual re-election.

3.4 Accountability

(a) Financial and business reporting (C.1)

The board should present a fair, balanced and understandable assessment of the company's position and prospects.

The board's responsibility in this regard extends to interim and other price-sensitive public reports and reports to regulators as well as information required to be presented by statute. The board should put in place arrangements which enable it to ensure that the information presented is fair, balanced and understandable.

The annual report should include a statement by the directors that they consider the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy.

An explanation of the basis on which the company generates or preserves value over the longer term and the strategy for delivering the objectives of the company should also be included in the annual report.

Finally, both the annual report and the half-yearly interim statement should include a statement by the directors as to whether they considered it appropriate to adopt the going concern basis of accounting in preparing them. This statement should identify any material uncertainties regarding the company's ability to continue to do so for at least 12 months from the date of approval of the relevant financial statements. [1]

(b) Risk management and internal control (C.2)

The board is responsible for determining the nature and extent of the principal risks it is willing to take in achieving its strategic objectives. The board should maintain sound risk management and internal control systems.

---

[1] The FRC has published additional guidance regarding the adoption of the going concern basis of accounting and the identification of any relevant material uncertainties - Guidance on risk management, internal control and related financial and business reporting (September 2014).

The annual report should include confirmation that the directors have carried out a robust assessment of the principal risks facing the company (including risks threatening its business model, future performance, solvency or liquidity) together with a description of those risks and an explanation of how they are being managed or mitigated.

An explanation should also be included in the annual report as to how the directors have assessed the prospects of the company and over what period they have done so. This explanation should be accompanied by a statement by the directors as to whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment. The directors should draw attention to any qualifications or assumptions underlying their expectation.

The statement referred to above is intended to express the directors' view about the longer term viability of the company over an appropriate period of time selected by the directors. The period to be covered by this viability statement will vary from company to company but, except in rare circumstance, it will be significantly longer than the 12 months required in respect of the going concern statement referred to in paragraph 3.4(a) above. In selecting the appropriate period, the directors should take into account, among other things, the nature of the company's business and its stage of development, its investment and planning periods and previous statements made by the directors (especially when raising capital).

The board should monitor the company's risk management and internal control systems (including financial, operational and compliance controls) and, at least once a year, carry out a review of their effectiveness. The annual report should include a report on that review. [2]

(c) **Audit committee and auditors (C.3)**

The board should establish formal and transparent arrangements for considering how they should apply the corporate reporting and risk management and internal control principles and for maintaining an appropriate relationship with the company's auditor.

The board should establish an audit committee of at least three (or, in the case of smaller companies, two) independent non-executive directors. In smaller companies, the company chairman may be a member of, but not chair, the

[2] Additional guidance regarding risk management and internal control has been published by the FRC - Guidance on risk management, internal control and related financial and business reporting (September 2014).

committee in addition to the independent non-executive directors, provided he or she was considered independent on appointment as chairman. At least one member of the audit committee should have recent and relevant financial experience.

The audit committee should review arrangements for staff of the company to raise, in confidence, concerns about possible improprieties in financial reporting or other matters. The objective should be to ensure that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action.

The audit committee should monitor and review the effectiveness of the internal audit activities. Where there is no internal audit function, the audit committee should consider annually whether there is a need for an internal audit function and make a recommendation to the board.

The audit committee should have primary responsibility for making a recommendation on the appointment, reappointment and removal of the external auditors. [3]

3.5 Remuneration

(a) The level and components of remuneration (D.1)

Executive directors' remuneration should be designed to promote the long-term success of the company. Performance-related elements should be transparent, stretching and rigorously applied.

The remuneration committee should judge where to position the company in relation to other companies but should use such comparisons with caution and should avoid paying more than is necessary. The committee should also be sensitive to pay and employment conditions elsewhere in the group, especially when determining annual salary increases.

Performance-related remuneration schemes for executive directors should include provisions that would enable the company to recover sums paid or withhold the payment of any sum and should specify the circumstances in which

[3] In addition to the guidance set out in the UK Corporate Governance Code, the FRC has published separate guidance designed to assist company boards in making suitable arrangements for their audit committees and to assist directors serving on audit committees in carrying out their role - Guidance on audit committees (September 2012).

the remuneration committee would consider it appropriate to apply these provisions.

Levels of remuneration for non-executive directors should reflect the time commitment and responsibilities of the role. Remuneration for non-executive directors should not include share options or other performance-related elements. If, exceptionally, options are granted, shareholder approval should be obtained in advance and any shares acquired on exercise should be held for at least one year after the non-executive director leaves the board. The holding of share options could be relevant to the determination of a non-executive director's independence.

The remuneration committee should carefully consider what compensation commitments would flow from the early termination of a director's appointment. The aim should be to avoid rewarding poor performance and to be robust in seeking to reduce compensation to reflect a departing director's obligation to mitigate his loss.

Notice or contract periods should be set at one year or less. Longer notice or contract periods which are necessary to recruit new outside directors should reduce to one year or less after the initial period.

(b) **Procedure (D.2)**

There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in deciding his or her own remuneration.

The chairman of the board should ensure that the committee chairman maintains contact as required with the company's principal shareholders about remuneration.

The board should establish a remuneration committee of at least three (or, in the case of smaller companies, two) independent non-executive directors. In addition, the chairman may also be a member of (but not chair) the committee if he or she was considered independent on appointment as chairman.

The remuneration committee should have delegated responsibility for setting remuneration for all executive directors and the chairman and should also recommend and monitor the level and structure of remuneration for senior management.

The board itself (or, if required by the articles of association, the shareholders) should determine the remuneration of the non-executive directors. If permitted by the articles, the board may delegate this responsibility to a committee.

Shareholders should be invited specifically to approve all new long-term incentive schemes and significant changes to existing schemes.

3.6 Relations with shareholders

(a) Dialogue with shareholders (E.1)

There should be a dialogue with shareholders based on the mutual understanding of objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders takes place.

The chairman should discuss governance and strategy with major shareholders and ensure that the views of shareholders are communicated to the board as a whole. Non-executive directors should have the opportunity to attend meetings with major shareholders and should expect to attend them if requested by major shareholders. The senior independent director should attend sufficient meetings with such shareholders to gain a balanced understanding of their issues and concerns.

(b) Constructive use of General Meetings (E.2)

The board should use general meetings to communicate with investors and to encourage their participation.

At any general meeting, a separate resolution should be proposed on each substantially separate issue. In particular, a resolution should be proposed at the AGM relating to the report and accounts. For each resolution, the proxy form should provide shareholders with the option to direct their proxy to vote either for or against the resolution or to withhold their vote. It should be made clear that a vote withheld is not a vote in law and will not be counted in the calculation of the proportion of the votes for and against the resolution.

The company should ensure that all valid proxy appointments received for general meetings are properly recorded and counted. For each resolution, where a vote has been taken on a show of hands, the company should ensure that details of the number of shares in respect of which proxy appointments have been validly made, the number of votes for and against the resolution and the number of shares in respect of which the vote was directed to be withheld are given at the meeting and made available as soon as reasonably practicable on the company's website. When a significant proportion of votes are cast against a resolution, the announcement of the vote result should be accompanied by an explanation of the action the company intends to take to understand the reasons behind the result. It is for the directors to determine what a significant proportion means for this purpose.

The chairmen of the various board committees should be available to answer questions at the AGM. All directors should attend the AGM.

Notices of meeting should be sent to shareholders, in the case of the AGM, at least 20 working days before the meeting and, in the case of other general meetings, at least 14 working days before the meeting.

4. THE NAPF SMALLER COMPANY GUIDELINES

4.1 Introduction

Whilst acknowledging that the UK Corporate Governance Code does not apply to AIM companies, the NAPF considers that the principles of the UK Corporate Governance Code are just as relevant to smaller quoted companies as they are to larger ones. Accordingly, boards of AIM companies are expected to be familiar with the main principles of the UK Corporate Governance Code and to seek to apply them as appropriate to their individual circumstances.

The NAPF Smaller Company Guidelines do not cover every provision of the UK Corporate Governance Code. Their purpose is to provide guidance to companies and shareholders on issues of key importance and where practice may reasonably differ from the UK Corporate Governance Code.

The NAPF expects companies at the top end of the AIM market capitalisation to comply with the provisions of the UK Corporate Governance Code (or to explain non-compliance) but also acknowledges that some AIM companies will be very small companies who can best serve their shareholders by concentrating on growing their business and providing good levels of disclosure in their annual report and accounts. All companies are expected to apply the highest standards of corporate governance consistent with the size and complexity of their business.

4.2 Disclosure standards

The NAPF emphasises that high quality disclosure is vital in order to achieve and maintain trust between a company and its shareholders and, accordingly, companies are encouraged to apply the disclosure standards set by the UK Corporate Governance Code. However, the NAPF acknowledges that this may be inappropriate for some small companies and specifies a minimum set of disclosures that it expects companies to make.

In addition to disclosures concerning the directors and the various board committees, these minimum disclosures include:

- a description of any board evaluation including the results and action taken or planned as a result;
- a business review which details the company's strategy and a summary of risk management;
- an audit committee report which reassures shareholders as to the maintenance of the auditor's independence; and
- a remuneration report which demonstrates alignment between the interests of senior management and shareholders (including a description of the performance hurdles of any incentive schemes).

4.3 NAPF AIM Policies

The NAPF Smaller Company Guidelines then proceed to set out the NAPF's policy for AIM companies in relation to certain key corporate governance issues as described below.

(a) *Combined roles of chairman and chief executive*

The NAPF AIM Policy supports the separation of the role of chairman and chief executive but acknowledges that a pragmatic approach is justified if a vote against the director combining these roles might be considered detrimental to the company.

(b) *CEO becoming chairman*

The NAPF AIM Policy is that succession of the CEO to chairman is acceptable only on rare occasions. Boards should consult their major outside shareholders before making such a decision and should also explain in the annual report how the board will ensure that it is not dominated by the individual so appointed.

(c) *Founder chairman or CEO*

Where the chairman and/or CEO is a founder and/or substantial shareholder (and/or founder who continues to have a large shareholding), the company should explain how the board ensures that decision making is not concentrated and that board oversight, and protection of all shareholders, is maintained, most appropriately in the form of a disclosed shareholder agreement.

(d) *Appointment of senior independent director*

The NAPF AIM Policy requires the appointment of a senior independent director where a company has a combined chairman and CEO in order to ensure that there is an independent voice on the board which can provide a communication channel for the company's shareholders if needed.

(e) *Balance of the board*

The NAPF AIM Policy requires, in the case of larger boards, at least two independent directors, excluding the chairman. In the case of smaller boards, there should be at least two independent non-executive directors to comprise not less than one third of the board, one of whom may be the chairman. The less stringent requirement applicable in the case of a smaller board is appropriate for AIM companies which have boards consisting of no more than four directors.

(f) *Composition of the audit, remuneration and nomination committees*

The NAPF AIM Policy supports the UK Corporate Governance Code requirements regarding the composition of the audit, remuneration and nomination committees but recognises that compliance may be unachievable in view of the lack of independent board members, compounded with the insufficient number of non-executive directors on a board.

The NAPF's position is therefore that the audit, remuneration and nomination committees should ideally comprise solely independent non-executive directors. As a minimum, there should be a majority of independent directors on all committees. The chairman may be a member of each committee provided that, other than his chairmanship, he fulfils the test of independence (in which case he will be viewed as an independent director).

(g) *Board evaluation*

The NAPF views board evaluation as an important tool for all boards and encourages companies to disclose details of any board evaluation process and, as far as possible, the outcomes from the evaluation.

(h) *Remuneration arrangements*

The NAPF's position is that companies should generally adhere to current best practice guidelines (that is, ABI & NAPF remuneration guidelines). A significant component of the remuneration of senior management should be linked to performance and there should be disclosure of the performance conditions attaching to any bonuses or long-term incentive plans. Companies are strongly encouraged to engage in constructive dialogue with their shareholders in relation to remuneration arrangements. It may also be appropriate to put their remuneration reports to a vote at the AGM.

(i) *Director independence*

The NAPF encourages companies to be rigorous in the assessment of director independence but recognises the need for a greater degree of flexibility in the case of AIM companies. The NAPF AIM Policy is that the independence of a director of an AIM company may be compromised if he has a beneficial or non-beneficial shareholding of more than three per cent in the company's issued share capital (as opposed to one per cent for FTSE All-Share companies).

(j) *Pre-emption rights*

The NAPF AIM Policy supports the Pre-emption Principles published in 2006 by the Pre-emption Group and companies should seek annual approval from shareholders for issuance on a non-pre-emptive basis.

However, the NAPF recognises that there may from time to time be good reasons for waiving pre-emption rights among smaller companies. Companies are encouraged to consult with leading shareholders in advance and provide them with a full justification for a decision to seek authority to issue stock above the 5 per cent annual limit. Any issuances above 10 per cent without pre-emption rights would need particularly cogent justification, unless prior approval has been sought.

This memorandum provides general guidance only in relation to the UK corporate governance environment for AIM companies and should not be used or relied on as a substitute for specific advice. If further general guidance is needed or if specific advice is needed in relation to a particular matter, you should contact Jeremy Landau at Rosenblatt Limited or Matt Davis at Spark Advisory, the nominated adviser.

Rosenblatt Limited

2021